

Message Text

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ACTION ARA-10

INFO OCT-01 ISO-00 SP-02 USIA-06 AID-05 EB-07 NSC-05
CIEP-01 TRSE-00 SS-15 STR-04 OMB-01 CEA-01 CIAE-00
COME-00 FRB-03 INR-07 NSAE-00 XMB-02 OPIC-03 LAB-04
SIL-01 IGA-02 DODE-00 PA-01 PRS-01 /082 W
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R 062015Z JAN 77
FM AMEMBASSY SANTIAGO
TO SECSTATE WASHDC 2881

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E. O. 11652: N/A
TAGS: EFIN, CI
SUBJECT: AUTHORITIES INTERVENE TO SAVE IMPORTANT SANTIAGO FINANCIAL
INSTITUTIONS

REF: SANTIAGO 22

1. ON JANUARY 5 THE CHILEAN CENTRAL BANK AND THE SUPERINTENDENCY
OF BANKS AND FINANCIAL INSTITUTIONS INTERVENED THE OSORNO
AND UNION BANK, ONE OF SANTIAGO'S LEADING FINANCIAL INSTITUTIONS.
THE BANK'S MANAGEMENT WAS ACCUSED OF UNSOUND ADMINISTRATIVE
PRACTICES. THE FORMER MANAGER OF FNCB'S SANTIAGO BRANCH WAS
DESIGNATED ADMINISTRATOR OF THE OSORNO AND UNION BANK.

2. THE DIRECTIVE ISSUED BY THE CENTRAL BANK ASSURED DEPOSITORS
AND FOREIGN LENDERS THAT THE CENTRAL BANK WILL PROVIDE THE
OSORNO AND UNION BANK WITH NECESSARY FINANCIAL ASSISTANCE.

3. COMMENT: FOR SEVERAL DAYS SANTIAGO HAS BEEN AWASH WITH
RUMORS OF AN INTERNAL STRUGGLE AT THE BANK INVOLVING UNSOUND
LENDING PRACTICES. THE INTERVENTION INDICATES THAT, WHATEVER
THE COST TO PUBLIC PURSE AND MONETARY OBJECTIVES, THE GOC IS
UNWILLING TO PERMIT AN IMPORTANT FINANCIAL INSTITUTION TO
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DEFAULT ON ITS DEBTS, ESPECIALLY IF SUCH FAILURE THEREATENS
TO MAR CHILE'S REPUTATION IN INTERNATIONAL FINANCIAL CIRCLES.
PRESUMABLY SMALLER FRY WILL SWIM OR SINK AS FREE MARKET FORCES
AND THEIR ABILITIES ALLOW. END COMMENT.

4. IN ANOTHER MAJOR MOVE TO SAVE A TOTTERING FINANCIAL SYSTEM,
PRESIDENT PINOCHET ANNOUNCED THAT THE GOC WILL GUARANTEE DEPOSITS

UP TO CH \$50,000 IN CHILEAN FINANCIAL INSTITUTIONS ("FINANCIERAS"). PRESUMABLY STATE GUARANTEES WILL NOT BE APPLIED TO UNREGISTERED FINANCIAL INSTITUTIONS WHICH REPUTEDLY ACCOUNT FOR A SUBSTANTIAL PART OF THE BUSINESS DONE IN THE CAPITAL MARKET. DEPOSITORS IN LA FAMILIA (REFTEL) AND OTHER INSOLVENT INSTITUTIONS, HE SAID, WOULD BE ALLOWED TO IMMEDIATELY WITHDRAW AMOUNTS OF UP TO CH \$50,000.

5. COMMENT: THE ECONOMIC OBJECTIVE OF THIS DECISION IS TO STOP THE RUN ON THE FINANCIAL INSTITUTIONS. BUT THIS DECISION COULD ALSO PROVE VERY EXPENSIVE, FINANCIALLY AND POLITICALLY. MANY OF THOSE INSTITUTIONS HAVE BEEN ENGAGED IN HIGHLY RISKY ACTIVITIES, A FACT WHICH THEIR DEPOSITORS SHOULD HAVE BEEN AWARE OF. INTEREST RATES REFLECTED THE RISK FACTOR AS WELL AS THE SHORTAGE OF SAVINGS IN RELATION TO DEMAND. THIS ACTION WILL ALSO PROVIDE GRIST FOR THE MILL OF THOSE OPPOSING GOC ECONOMIC POLICY. IN BAILING OUT A PARTICULAR CLASS OF INVESTOR THE GOC GOES AGAINST ITS OWN TENETS ABOUT THE SAME RULES OF THE GAME FOR ALL. IT WOULD ALSO APPEAR TO BE TACIT ADMISSION THAT GOC ECONOMIC POLICY HAS BEEN AT FAULT FOR THE PRESENT MESS IN THE CAPITAL MARKET. POLICYMAKERS HAD ARGUED THE GREAT BENEFITS OF CAPITAL MARKET DEVELOPMENT TO THE PUBLIC BUT HAD FAILED TO COUNSEL IT ON THE RISKS.

6. THE DECISION TO ALLOW IMMEDIATE WITHDRAWALS AT INSOLVENT INSTITUTIONS IS OBVIOUSLY DESIGNED TO HEAD OFF FURTHER DAMAGING REVELATIONS IN THE CASE OF LA FAMILIA TO GOC AND GOC SUPPORTERS, WHICH A JUST INITIATED COURT SUIT WOULD HAVE DONE. HOW FAR THE GOC WILL BE WILLING TO GO TO KEEP THE LID ON THIS SORDID AFFAIR REMAINS TO BE SEEN.

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Message Attributes

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Sent Date: 06-Jan-1977 12:00:00 am
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